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7
8 Attorneys for Debtor

9 UNITED STATES BANKRUPTCY COURT

10 DISTRICT OF OREGON

11 In re

12 Peak Web LLC,

13 Debtor.

Case No. 16-32311-pcm11

**DECLARATION OF MARK
CALVERT OF CASCADE CAPITAL
GROUP IN SUPPORT OF DEBTOR'S
FIRST DAY MOTIONS**

15 I, Mark Calvert, declare under penalty of perjury under the laws of the United
16 States of America that the following is true and correct to the best of my knowledge and
17 belief, that I am competent to testify to the matters stated herein, and that I understand they
18 are made for use as evidence in court and are subject to penalty for perjury.

19 1. I, through Cascade Capital Group ("Cascade"), was retained by Peak
20 Web LLC, dba Peak Hosting ("Peak," "Peak Hosting," or "Debtor") to be the Chief
21 Restructuring Officer (CRO) of Peak. I am a Certified Public Accountant (CPA), Certified
22 Insolvency and Recovery Advisor (CIRA), Certified Turnaround Professional (CTP), and a
23 Certified Fraud Examiner (CFE). I have also been appointed by the courts as a trustee for a
24 number of companies in bankruptcy. In addition, I have been appointed as a referee by the
25 court. I have over 25 years of experience working with troubled companies, and in the past
26 10 years have restructured in excess of \$5 billion in debt in and outside of formal bankruptcy

1 proceedings. Currently I have five companies in bankruptcy in which I am either the
2 receiver, trustee, or CRO.

3 2. I submit this declaration to assist the Court and other parties-in-interest
4 in understanding the circumstances that compelled the commencement of this Chapter 11
5 case and in support of Peak's various motions and applications filed with the Court
6 contemporaneously herewith. Except as otherwise indicated, all facts set forth in this
7 declaration are based on my personal knowledge; my review of relevant documents; or my
8 opinion based upon my experience, knowledge, and information concerning Peak's
9 operations and financial affairs. If called upon to testify, I would testify to the facts set forth
10 in this Declaration.

11 3. In early May, Cascade was retained to complete an assessment of
12 Peak's operations and to assess the viability of the company's ongoing out-of-court
13 restructuring that began in January 2016. Based on the limited remaining cash available if all
14 payments are made in accordance with contract terms and the inability to get all 25-plus
15 lessors and lenders to restructure their debts, Cascade determined that Peak needs to
16 complete the balance of its restructuring in a formal Chapter 11 bankruptcy.

17 4. On June 13, 2016 (the "Petition Date"), Peak filed its voluntary
18 Petition for relief under Chapter 11 of Title 11 of the United States Code. The Chapter 11
19 will allow Peak to restructure its debt obligations consistent with its downsized operations
20 while allowing it to aggressively prosecute the Litigation described below. The Chapter 11
21 will permit Debtor to maximize the potential recovery for all its creditors.

22 5. Promptly after filing its Chapter 11 petition, Peak filed certain
23 applications, motions, and proposed orders (the "First Day Motions"). Peak requests that
24 orders for each of the First Day Motions be entered, as each constitutes a critical element in
25 achieving a successful reorganization of Peak for the benefit of all parties-in-interest.
26

1 **BACKGROUND**

2 6. Peak is a California limited liability company authorized to transact
3 business in various jurisdictions, including the State of Oregon, and is headquartered in
4 Oregon.

5 7. Peak is a managed-service company that provides the servers, storage,
6 network, datacenter, and staff for some of the largest online businesses. Peak is essentially a
7 "cloud" service provider for companies that do not want to build out an operations
8 department to run all these elements themselves.

9 8. In addition to me, Peak's leadership team is comprised of (a) Jeffrey
10 Papen, Chief Executive Officer and founder; (b) Lisa Bunday, Chief Financial Officer; and
11 (c) Shara Wokal, Director of Human Resources; (d) Jon Billow, Chief Technology Officer,
12 all of whom are located in Oregon;

13 9. Peak has received multiple awards. These include being selected
14 (a) as a 2015 finalist for the Technology Association of Oregon's Growth Technology
15 Company of the Year; (b) among the best managed-hosting providers by HostReview; (c) as
16 an innovative managed-service provider by CRN; (d) among the top managed-services
17 provider executives, entrepreneurs, and experts by MSPmentor; (e) as a finalist in the
18 "innovations in the outsourced environment" category by DatacenterDynamics; and
19 (f) among the top 20 best cloud hosting companies by Serchen. Peak was named a silver
20 winner in Fastest-Growing Company of the Year for the 2015 Best in Biz Awards.

21 10. Peak uses its confidential and proprietary trade secret technology and
22 knowhow to create network architectures that support the growth and volume of user data
23 exchanged, stored, and processed through its clients' network applications. The complex
24 network architectures are designed and built by Peak and have thousands of physical
25 components and corresponding software that are uniquely configured to operate online
26 applications at high rates of speed without latency, jitters, corruption, or failure. Peak

1 developed its trade secret network architecture over more than 15 years, with tens of
2 thousands of engineering and architectural hours, and millions of dollars invested in its
3 research and development.

4 11. Peak was founded by Mr. Papen in 2001. Over the course of 13 years,
5 Peak's revenue grew to approximately \$1 million per month. Starting in 2013, a single
6 customer, Machine Zone, grew Peak to \$5 million in revenue per month over a 14-month
7 period. To support Machine Zone, Peak purchased over \$35 million in hardware
8 (approximately \$25 million of which was guaranteed by Mr. Papen) and significantly
9 increased its staff. By 2015, Peak employed approximately 185 people and had data centers
10 in six locations across the United States and one in Europe.

11 12. Machine Zone is the developer of Game of War and Mobile Strike,
12 mobile gaming apps that are played by millions of people around the world who talk,
13 collaborate, and compete in an expansive virtual environment 24 hours a day, seven days a
14 week, using their handheld devices. Although free to download, the game is designed to
15 encourage players to make in-game purchases to gain power and more quickly advance
16 through the game. Game of War was an instant success and is one of the top grossing mobile
17 gaming apps, generating millions of dollars in revenue per day and \$600 million annually.
18 Machine Zone grew rapidly and had a purported valuation of \$3 billion in 2014.

19 13. Peak's network architecture is particularly valuable to Machine Zone
20 because of Peak's thousands of unique design choices, configurations, and command codes
21 that improve Game of War's speed and reliability, both of which are critical to Game of
22 War's success and profitability.

23 **EVENTS LEADING TO BANKRUPTCY**

24 14. Pursuant to the parties' written non-disclosure and network hosting
25 agreements, Machine Zone used Peak's proprietary and trade secret network architecture. In
26 exchange, Machine Zone agreed to pay Peak monthly recurring charges of approximately

1 \$4.08 million through at least October 1, 2017. Machine Zone also agreed that if it
2 terminated the agreement early for convenience, Machine Zone was required to pay the
3 remaining recurring monthly payments through the full term of the agreement.

4 15. Shortly after the parties' executed an extended network hosting
5 agreement in February 2015, Machine Zone induced Peak Hosting to allow Machine Zone to
6 copy its trade secret network architecture by falsely representing that it was building a
7 backup data center in Las Vegas to serve as a recovery source in the event of a disaster to
8 Peak Hosting's primary data center in Dallas. All the while, Machine Zone repeatedly
9 assured Peak that it was a gaming company and not an operations company, and that it had
10 no interest in bringing the operations services Peak was providing in-house to Machine Zone.
11 Accordingly, pursuant to Machine Zone's representations and the parties' written agreements,
12 Peak provided Machine Zone with its trade secret network topology, configurations,
13 command codes, and other confidential knowhow that Machine Zone copied to build an
14 identical network architecture in Machine Zone's Las Vegas data center.

15 16. On October 27, 2015, a previously unknown and undocumented Cisco
16 software bug caused a Cisco Nexus switch in Peak's network system to malfunction,
17 resulting in a Game of War outage that lasted a little over two hours. Cisco, a third-party
18 vendor, has repeatedly confirmed in writing that the initial outage, and subsequent outages in
19 November, were Cisco's fault and caused by the software bug ID CSCux02122 in its Nexus
20 switch. Cisco has since released a software patch to fix the bug. The Machine Zone
21 agreement expressly provides that: (a) Peak is not responsible for network outages caused by
22 vendor software bugs, and (b) a single outage is not grounds to terminate the agreement.
23 Nevertheless, on October 28, 2015, the day after the network outage, and without knowing
24 what caused the outage, Machine Zone used the single outage as an excuse to wrongfully
25 terminate the parties' agreement. Machine Zone terminated the agreement early and without
26 cause because it had already obtained and used Peak's trade secrets, confidential information,

1 and technical knowhow to duplicate Peak's network system and manage its network
2 operations in-house.

3 17. Machine Zone gave written notice of termination on October 29, 2015,
4 but demanded that Peak continue to operate Game of War through its Dallas data center until
5 December 27, 2015. This gave Machine Zone sufficient time to transfer Game of War to its
6 Las Vegas data center without incurring significant revenue loss by taking the game offline
7 for several weeks. Although Peak could have shut down Game of War's network operations
8 after being wrongfully terminated, costing Machine Zone tens of millions of dollars in lost
9 revenue, Peak continued to provide network hosting services in good faith until
10 December 27, 2015. In doing so, Peak incurred substantial overhead costs which otherwise
11 would not have been necessary. In return, Machine Zone concealed for months that it never
12 intended to pay Peak the millions of dollars owed for October, November, or
13 December 2015.

14 18. Machine Zone was 80% of Peak's business, and Peak relied on
15 Machine Zone's promise to pay the \$4.08 million in monthly recurring network hosting
16 charges through the full term of the agreement. By continuing to provide network hosting
17 services in good faith through December 27, 2015, Peak incurred substantial overhead costs
18 which otherwise would not have been necessary. Machine Zone has still not paid for the
19 services provided by Peak. In addition, the agreement provides that because Machine Zone
20 terminated the agreement for convenience, Machine Zone must pay Peak the full
21 \$85.7 million owed for the remaining term of the agreement (January 1, 2016 through
22 October 1, 2017), for a total of \$96.7 million in damages. Further, although the agreement
23 requires Machine Zone to cease all use of Peak's trade secrets and confidential information
24 upon termination of the agreement, regardless of whether it was terminated for cause or
25 convenience, Machine Zone is continuing to use Peak's trade secrets and confidential
26 information without authorization.

1 19. In November of 2015, Peak Hosting and Machine Zone entered into
2 cross lawsuits in the Superior Court of the State of California, County of Santa Clara, with
3 respect to the above facts (collectively, the "Litigation"). Mr. Papen and others at Peak have
4 spent the last six-plus months, and will continue to spend significant time, participating in the
5 Litigation and pursuing a judgment against Machine Zone.

6 20. Machine Zone's departure in December of 2015 resulted in a dramatic
7 downsizing for Peak given it had spent the last two years ramping up to service Machine
8 Zone. Since January, Peak has been working on an out-of-court restructuring with the
9 25-plus lessors and secured lenders. The company has closed down seven data centers and
10 consolidated operations into one data center. Peak had to reduce its workforce from
11 approximately 185 people to around 50 people in the past five months. In addition, Peak
12 spent considerable time analyzing its current equipment needs and has been working with
13 each lessor or secured lender to return equipment no longer required. Peak has also vacated
14 unnecessary office space and restructured its data center lease.

15 21. The significant cuts that have been made prior to the bankruptcy filing
16 have reduced the size of the company back to approximately the same size as before the
17 Machine Zone contract. Key personnel necessary to pursue the Litigation have been retained
18 and remain available to support the ongoing Litigation. A restructured Peak will be able to
19 generate sufficient revenue to become profitable again and generate a return to creditors.
20 However, the company will need financing (which has been obtained) to support operations
21 and to fund the Litigation. A successful result in the Litigation will be an additional source
22 of recovery for Peak's creditors.

23 22. The secured lender, Bank of the West ("BOTW"), and Peak have
24 discussed a proposed cash collateral arrangement and the funding needed for the Litigation.
25 Debtor believes it will present agreed-upon orders with BOTW at the initial court hearing on
26 those motions.

1 **CURRENT OPERATIONS**

2 23. Peak has done the hard work of reorganizing its staffing, equipment,
3 and space needs, while continuing to provide dedicated equipment and elite support staff to
4 its customers at all times. It currently has 54 employees who average 13 years of experience
5 in the industry, the majority of whom are technical engineering staff specializing in highly
6 scalable, available internet-based infrastructure technologies. Peak's employees are
7 committed to understanding customers' businesses and creating the best managed hosting
8 solution. Peak remains headquartered in Oregon; it currently has a data center in Santa
9 Clara; and it is storing equipment to be returned to lessors and lenders in Fremont, California.

10 24. Pre-filing, Peak returned a significant portion of excess equipment and
11 is well positioned to complete the process in the first few weeks of the bankruptcy. The first
12 day motions include a motion to reject unnecessary executory contracts and leases, provide
13 for the immediate return of equipment, and provide lessors and lenders with relief from the
14 automatic stay to liquidate the equipment in a commercially reasonable manner. The
15 bankruptcy case will allow the company to complete the out-of-court restructuring process
16 started back in January.

17 25. Peak's operations and engineering teams currently support 26
18 customers in industries spanning online and mobile gaming, finance, real estate, consulting,
19 and big data companies. Peak has 50% of its data center pre-built and ready for new
20 customers. This equates to about 100 racks of space, which can accommodate approximately
21 2,000 additional servers for the expansion of new and existing customers.

22 26. In addition to providing excellent service to its customers, Peak will
23 use the Chapter 11 process to restructure its debt with lessors and lenders. Peak currently has
24 three term loans with BOTW: one equipment line of credit, one revolving line of credit, and
25 one non-revolving line of credit, totaling approximately \$6.2 million. Peak is working with
26 BOTW and hopes to reach a consensual restructuring of BOTW's debt.

1 27. Peak has operating and capital equipment leases with various lessors
2 and lenders. Much of the equipment Peak leased or financed was procured to support its
3 work for Machine Zone. As a result of Machine Zone's departure, a significant portion of
4 the equipment is no longer needed. Over the past five months the company has
5 (a) determined which equipment it would like to retain, (b) inventoried the equipment,
6 (c) placed the equipment on pallets on a lessor-by-lessor basis, and (d) placed the equipment
7 at a shipping and receiving facility ready for pick-up. Many creditors have already taken
8 possession of their collateral. Peak is rejecting the leases it does not intend to retain as of the
9 Petition Date because it no longer needs the equipment subject to those leases. In addition,
10 the current plan is to accept certain leases Peak does need in the near future.

11 28. In order to maintain operations as it reorganizes, Peak requires post-
12 petition loans. Peak has negotiated a \$500,000 post-petition unsecured line of credit from
13 PSA 9, LLC ("PSA 9"). Peak will use these funds, as needed, to pay ordinary operating
14 expenses as and when they come due and to maintain adequate operating capital for
15 stabilized operations. PSA 9 is affiliated with the entity that holds a 20% equity interest in
16 Debtor.

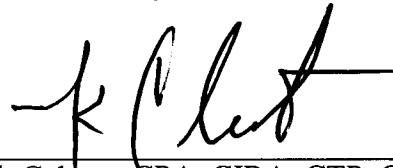
17 29. Further, Peak is seeking this Court's authority to continue the
18 employment of Susman Godfrey LLP ("Susman") and Ropers Majeski Kohn Bentley PC
19 ("Ropers") as its litigation counsel in the Machine Zone Litigation. Peak has been working
20 with Ropers, counsel hired by Peak's insurance company, for a number of months. Peak
21 recently also engaged Susman, a nationally-recognized firm that focuses on high-stakes
22 commercial litigation. Susman is so confident in Peak's case against Machine Zone that it
23 has agreed to take the case on a contingent-fee basis. Although the contingent fee
24 arrangement significantly reduces the professional legal fees that must be paid during the
25 course of the case, there will still be significant out-of-pocket costs associated with the
26 retention of experts and other related costs that must be paid as the case proceeds.

1 30. In order to pay the litigation costs necessary to pursue the Litigation,
2 Peak required additional financing. Prior to the Petition Date, Peak obtained a secured line
3 of credit from PSA 9 in the amount of \$1.5 million to finance the costs of the Litigation.
4 Fifty thousand dollars was advanced pre-petition. An additional \$150,000 will need to be
5 advance by June 30, 2016. This loan and the aforementioned unsecured operating line of
6 credit, reflect the extent to which Peak's owners believe in Peak, its long-term viability, and
7 its ability to prevail in the Litigation. The Litigation loan is required to have a first priority
8 security interest position in the Litigation and proceeds thereof. Based on preliminary
9 discussions with BOTW, it appears BOTW will consent to a priming lien on the Litigation.
10 To the extent other creditors assert liens on the Litigation proceeds, their liens are avoidable
11 as preferences or otherwise, and in any event will be primed to the extent necessary prior to
12 the avoidance of their liens. It should be noted that the waterfall for the Litigation proceeds
13 will go first to PSA 9 to repay its secured Litigation loan, then to BOTW, and the balance to
14 pay unsecured creditors up to the full amount of their debt.

15 31. The current plan is to move the case forward on a timely basis. Peak
16 expects to file a plan of reorganization within the original exclusivity period.

17 **I DECLARE UNDER PENALTY OF PERJURY THAT THE**
18 **FOREGOING IS TRUE AND CORRECT.**

19 This Declaration was executed on this 13th day of June, 2016.

20
21 

22 _____
Mark Calvert, CPA, CIRA, CTP, CFE and PI

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